
Joint Enforcement Strike Force

On the Underground Economy

2016 REPORT

This report was prepared by the Tax Branch of the California Employment Development Department (EDD).

Lisa M. Wheeler, Deputy Director, Tax Branch
Clara Yen, Chief, Field Audit and Compliance Division
Mike Lee, Chief, Compliance Development Operations

For more information, please call 916-227-2730.

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The Honorable Members of the California State Legislature
California State Senate and Assembly
State Capitol
Sacramento, CA 95814

Dear Members of the California State Legislature:

Executive Order W-66-93 established the Joint Enforcement Strike Force (JESF) on the Underground Economy to combat the underground economy by pooling resources and sharing data among the state agencies charged with enforcing licensing, labor, and payroll tax laws. On January 1, 1995, Section 329 was added to the California Unemployment Insurance Code (CUIC), which placed the provisions of the Executive Order into law. This section contains a provision requiring the strike force to report to the Governor and the Legislature annually regarding its activities. This letter is being sent pursuant to Government Code Section 9795(a) that requires each legislative mandated report to include a summary of its contents not to exceed one-page in length, which is distributed to each member of the Legislature.

The JESF 2016 Report provides the annual summary of activities and outcomes from the JESF in accordance with Section 329(d) of the CUIC. This report includes the following contents:

- An overview of the JESF including information about strike force partners.
- Background information about the underground economy and the JESF's goals.
- Efforts made by the strike force to publicize its activities and to receive referrals from the public including web page view statistics.
- Informant contact statistics for the toll-free JESF hotline and other outlets.
- Narrative information about collaboration among the strike force partners and statistical results from collaborative efforts.
- Statistics and narratives about blatant violations and noncompliance with licensing, labor and payroll tax laws identified, audited, investigated, or prosecuted through civil actions or criminal prosecution.

Printed copies of this report are available to any legislative member upon request. The report can also be viewed online at www.edd.ca.gov/About_EDD/EDD_Legislative_Reports.htm.

Sincerely,

/s/ PATRICK W. HENNING
Director

JOINT ENFORCEMENT STRIKE FORCE OVERVIEW, MEMBERS, AND PARTICIPATING ENTITIES

This legislatively mandated report provides the annual summary of activities and outcomes from the Joint Enforcement Strike Force (JESF) on the Underground Economy in accordance with Section 329(d) of the California Unemployment Insurance Code (CUIC). In October 1993, Executive Order W-66-93 established the JESF to combat the underground economy by pooling resources and sharing data among the state agencies charged with enforcing licensing, labor, and payroll tax laws.

On January 1, 1995, Section 329 was added to the CUIC, which placed the provisions of the Executive Order into law. The Employment Development Department (EDD) is the designated lead agency of the JESF, and the EDD Director or designee serves as its chair. The JESF members are as follows:

The **EDD – Tax Branch** works with employers to collect California’s payroll taxes and data to support the employment security, child support, and personal income tax programs. The Tax Branch is committed to providing service to California employers and Unemployment Insurance (UI), Disability Insurance (DI), and Paid Family Leave benefit claimants; and to increasing voluntary compliance with payroll tax laws through education, simplified reporting processes, and the promotion of fair business competition. The Tax Branch’s **Compliance Development Operations** program is responsible for coordinating the EDD’s efforts at combating the underground economy and is also responsible for leading and coordinating the activities of the JESF as a whole.

The **EDD – Investigation Division (ID) Criminal Tax Enforcement Program** is a specialized law enforcement unit that investigates criminal violations of the CUIC, the California Penal Code (PC), and the United States Code for federal prosecutions. The ID conducts surveillance, performs undercover operations, interviews witnesses, initiates search warrants, and submits completed investigations to prosecutors to convict individuals who commit payroll tax fraud. The EDD determines if the convicted party made restitution, is still on active probation, and obeys all laws with respect to the future filing of returns and payments. The conviction itself and the collection of the tax liabilities play an integral part in deterring the underground economy. The EDD also collaborates on workers’ compensation insurance investigations related to state payroll tax violations. The ID, Tax Branch, and UI Branch work together to address fictitious employer schemes created to perpetrate fraud against the EDD. They identify potential fictitious employer schemes based on thorough and ongoing evaluation of the characteristics and elements of such schemes. The identification of these fictitious employer schemes allows the EDD to increase detection and elimination of fraudulent UI and DI benefit claims filed against the EDD.

The **Department of Consumer Affairs (DCA)** protects and serves California consumers and ensures a competitive and fair marketplace. The DCA helps consumers learn how to protect themselves from unscrupulous and unqualified individuals. The

DCA protects professionals from unfair competition by identifying unlicensed practitioners.

The **DCA – Contractors State License Board (CSLB)** protects consumers by licensing and regulating California's construction industry. There are approximately 300,000 licensed contractors in the state, in 43 different licensing classifications. In addition to consumer education on contractor and construction law, CSLB activities include: administer prospective licensee examinations; issue licenses; investigate complaints against licensed and unlicensed contractors; issue citations; suspend or revoke licenses; and seek administrative, criminal, and civil sanctions against violators.

The **CSLB's Statewide Investigative Fraud Team** is set up to monitor and combat illegal activity. They have teams throughout the state that conduct sting operations on a regular basis and sweep construction sites. They also conduct joint operations and sweeps with other state agencies dedicated to combatting the underground activity.

The **DCA – Bureau of Automotive Repair (BAR)** investigates general auto repair complaints and ensures that shops comply with Smog Check statutes. Each year, the BAR handles more than 14,800 complaints related to auto repair and/or Smog Check inspections. The BAR staff investigates complaints and negotiates with the shop on the consumer's behalf to achieve a mutually agreeable resolution. The bulk of complaints are resolved by mediation. Each year, the BAR returns over \$6 million to California consumers in the form of direct refunds, rework, or adjustments.

The **DCA – Bureau of Security and Investigative Services (BSIS)** protects consumers by licensing and regulating the following industries: alarm company operators and alarm company employees, locksmith companies and locksmith company employees, private investigators, private patrol operators and security guards, proprietary private security employers and officers, reposessor agencies and reposessor agency employees, and training facilities and training instructors. As part of its mission, the BSIS actively investigates complaints against its licensees and works to punish unlicensed business operations. This includes the suspension and revocation of licenses and seeking administrative, criminal, and civil sanctions against violators. Undercover sting and sweep operations are conducted on an ongoing basis throughout California. The BSIS also educates consumers, administers examinations to validate prospective licensees, and issues licenses and permits.

The **Department of Industrial Relations (DIR) - Division of Labor Standards Enforcement's (DLSE), Bureau of Field Enforcement** is responsible for the investigation and enforcement of statutes covering workers' compensation insurance coverage, child labor, cash pay, unlicensed contractors, Industrial Welfare Commission orders, and group claims involving minimum wage and overtime claims. The Bureau of Field Enforcement also handles criminal investigations involving these group claims.

The **DIR – Division of Occupational Safety and Health's (DOSH) (Ca/OSHA)** enforcement unit has jurisdiction over every employment situation and place of

employment in California, which is necessary to adequately enforce and administer all occupational safety and health standards and regulations. They conduct inspections of California workplaces in response to a report of an industrial accident, a complaint about an occupational safety and health hazard, or as part of an inspection program targeting industries which have a high rate of occupational hazards, fatalities, injuries, or illnesses.

The **California Department of Insurance (CDI)** ensures that consumers are protected; the insurance marketplace is fostered to be vibrant and stable; the regulatory process is maintained as open and equitable; and the law is enforced fairly and impartially. The **Fraud Division** is charged with investigating insurance fraud, which includes the crimes of intentional misrepresentation of payroll and employee staffing in order to obtain lower rates for workers' compensation insurance. Studies suggest that the aggressive anti-fraud campaign by the CDI, the district attorneys, the insurance industry, and California employers continue to play a substantial role in reducing crime and help lower workers' compensation insurance premiums for employers statewide.

The **Franchise Tax Board's (FTB)** primary function is to administer the California Revenue and Taxation Code (R&TC). Elected officials determine the tax policy for raising revenue. Under the direction of the FTB's Chief Law Enforcement Officer, the **Criminal Investigation Bureau (CIB)** enforces the criminal provisions of the R&TC. The CIB's principal mission is to identify, investigate, prosecute, and deter tax evasion and fraud, and encourage compliance with California income tax laws while maintaining the public's trust through publicity. The CIB takes over where voluntary compliance and civil enforcement efforts end. Special agents with full peace officer powers investigate alleged criminal violations of the R&TC, principally income tax fraud and evasion, and assist in prosecuting non-compliant individuals. The special agents' efforts are supported by forensic auditors, collectors, analysts, and support staff; basically a micro-organization all in one bureau. The CIB also relies on a strong collaborative enterprise to accomplish their mission.

The **Board of Equalization (BOE)** administers tax programs in four general areas: sales and use taxes, property taxes, special taxes and fees, and the tax appellate program. The BOE's **Investigations Division** plans, organizes, directs, and oversees all criminal investigative activities for the various programs administered by the BOE. Its goals are to identify tax evasion and new fraud schemes and actively investigate and assist in the prosecution of individuals who are violating the laws administered by the BOE.

The **Department of Justice** Attorney General works to protect California's workers, legitimate businesses, and taxpayers through the **Underground Economy Unit**. The Underground Economy Unit brings civil and criminal actions against persons engaged in the underground economy. It has used California laws to obtain restitution of unpaid wages, civil penalties, and injunctions to bring businesses into compliance with applicable labor, tax, and licensing laws. These enforcement efforts deter underground economy violations, recapture lost revenues, and protect workers and legitimate

businesses from illegal and predatory enterprises. The Underground Economy Unit has prosecuted cases involving: wage, tax, and insurance issues including the theft of wages, unpaid overtime, denial of breaks, payroll tax evasion, and misclassification of employees as independent contractors; patterns of safety violations leading to fatal workplace injuries; workers' compensation insurance premium fraud; and the illegal avoidance of workers' compensation coverage for employees.

The **California Department of Alcohol Beverage Control's (ABC)** agents are peace officers under Section 830.2 of the California PC and are empowered to investigate and make arrests for violations of the Business and Professions Code that occur on or about licensed premises. Agents are further empowered to enforce any penal provisions of the law in the state. Licensees who violate state laws or local ordinances are subject to disciplinary action and may have their licenses suspended or revoked. These licensees are entitled to a hearing before an Administrative Law Judge and an appellate process to the State Supreme Court.

The **United States Department of Labor's (USDOL)** mission is to foster, promote, and develop the welfare of the wage earners, job seekers, and retirees of the United States; improve working conditions; advance opportunities for profitable employment; and assure work-related benefits and rights. The **Fair Labor Standards Act** prescribes standards for wages and overtime pay, which affect most private and public employment. The act is administered by the **Wage and Hour Division**. It requires employers to pay covered employees, who are not otherwise exempt, at least the federal minimum wage and overtime pay of one and one-half times the regular rate of pay. For non-agricultural operations, it restricts the hours that children under age 16 can work and forbids the employment of children under age 18 in certain jobs deemed too dangerous. For agricultural operations, it prohibits the employment of children under age 16 during school hours and in certain jobs deemed too dangerous. The Wage and Hour Division also enforces the labor standards provisions of the **Immigration and Nationality Act** that apply to aliens authorized to work in the United States under certain non-immigrant visa programs (H-1B, H-1B1, H-1C, H-2A).

The **United States Internal Revenue Service's (IRS)** mission is to serve America's taxpayers by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all. In fiscal year 2016, the IRS collected \$3.3 trillion in taxes (gross tax receipts before tax refunds of \$426 billion) and processed over 244 million tax returns and other forms. The IRS provides EDD with leads that are used for various JESF activities, including investigating employers with unreported wages and/or misclassified workers

BACKGROUND AND PROGRAM INFORMATION

The Underground Economy

“America has two economies, and one is flourishing at the expense of the other. First, there’s the legitimate economy, in which craftsmen are licensed and employers and employees pay taxes. Then there’s the fast-growing underground economy, where millions of workers are paid off-the-books, their incomes largely untaxed.”

--“Going Underground”, Barron’s Online, January 3, 2005

The size of the underground economy is difficult to measure but the following data points help to illustrate its magnitude:

- A 2012 study by the economist Edgar Feige at the University of Wisconsin estimated that underground activity in the United States totaled as much as \$2 trillion.
- The tax gap is defined as the amount of tax liability faced by taxpayers that is not paid on time. Tax gap estimates for tax year 2006, released by the IRS in 2012 and adjusted for audit and collection activities, estimate that in 2006 the net national tax gap was approximately \$385 billion.
- In its March 2015 report, California’s Little Hoover Commission indicated, “The underground economy also robs the state of an estimated \$8.5 billion to \$10 billion in uncollected tax revenue, money that could fund education, law enforcement or long-overdue infrastructure investments or reduce taxes for the majority of Californians who play by the rules.”

Reports on the underground economy indicate it imposes a significant burden on revenue needed to fund critical state programs and businesses that comply with the law. When businesses operate in the underground economy, they gain an unfair, competitive advantage over businesses that comply with labor, licensing, and payroll tax laws. This causes unfair competition in the marketplace and forces law-abiding businesses to pay higher taxes and expenses due to socialized costs.

Workers of non-compliant businesses are also affected. Their working conditions may not meet the legal requirements, which can put them in danger. Their wage earnings may be less than what is required by law, and benefits they are entitled to can be denied or delayed because their wages are not properly reported. Consumers can also be affected when contracting with unlicensed businesses. Licensing provisions are designed to ensure sufficient skill and knowledge to protect consumers.

Joint Enforcement Strike Force Goals

The JESF's goals are to help restore economic stability and to improve working conditions and consumer and worker protection in the state. Specifically, the JESF works to:

- Eliminate unfair business competition.
- Protect workers by ensuring that they receive all compensation, benefits, and worker protections they are entitled to by law relating to their employment.
- Protect consumers by ensuring that all businesses are properly licensed and that they adhere to the state's consumer protection regulations.
- Reduce the burden on law-abiding citizens and businesses by ensuring that all businesses and individuals comply with the state's licensing, regulatory, and payroll tax laws.
- Reduce the tax gap by increasing voluntary compliance with the state's payroll tax laws to maximize the state's General and Special Funds.

INFORMATION REQUIRED BY SECTION 329(d) OF THE CALIFORNIA UNEMPLOYMENT INSURANCE CODE

Informant Contacts

Allegations of violation of payroll tax, labor, and licensing laws may be reported by telephone to the toll-free JESF hotline at 800-528-1783. Informants may also submit information about state payroll tax fraud by completing a [Fraud Reporting Form](#) online via the EDD website, via e-mail to ueo@edd.ca.gov, via correspondence by fax to 916-227-2772 or by completing and mailing an *Underground Economy Operations Lead Referral/Complaint Form*, available in English ([DE 660](#)) and Spanish ([DE 660/S/](#)). In 2016, the EDD received a total of 3,444 allegations:

- 1,112 allegations via telephone calls to the JESF hotline.
- 2,121 allegations via online submission (EDD website or email).
- 211 allegations via correspondence (fax or mail).

Publicity and Marketing Outreach Strategies

The JESF publicizes its activities, outreach, and education on the underground economy through the following:

- The [Joint Enforcement Strike Force website](#) received 1,108 page views in calendar year 2016. It was created to:
 - Provide information on how to report fraud to the JESF.
 - Educate readers about the harm caused by the underground economy.
 - Publicize the work being done by California state government and partner agencies.
 - Deter fraudulent activity by communicating that California state government will actively pursue and punish those who participate in the underground economy.
 - Provide contact information for each of the partner agencies.
- Information on the underground economy is included on the following website: **www.edd.ca.gov/Payroll_Taxes/Underground_Economy_Operations.htm**. It provides the viewer with data, access to prior reports, program and operation information, etc. In calendar year 2016, the website received 5,623 page views.
- The EDD has a web section dedicated to [fraud and penalties](#). It provides information so that both benefit recipients and employers can avoid serious costs and consequences by learning more about their roles and responsibilities when it comes to providing required information for collecting benefits or reporting employee data. In calendar year 2016, it received 79,177 page views. Within the fraud and penalties section is a special page dedicated to informing the public about cases the EDD is involved with for [prosecuting fraud](#). In calendar year 2016, it received 53,374 page views.
- From time to time, the EDD includes articles about efforts to combat the underground economy in its *California Employer* newsletter and internally in the *Scene* employee newsletter. The *California Employer* newsletter, first quarter of 2016 edition, included an article about partnering efforts to combat the underground economy titled, *EDD Collaborates With State, Federal Agencies to Combat Fraud, Unfair Business Practices*.
- The Small Business Employer Advisory Committee is a group of diverse associations representing small business employers throughout California. The committee interactively provides the EDD with recommendations on how to better serve California's small businesses and disseminates information to their respective members. The EDD gave a presentation on fraud deterrence, prevention, and detection and the underground economy at the committee's May 12, 2016 meeting in Sacramento.
- A variety of information sheets and publications are available to the public, businesses, and taxpayers. These publications include:
 - *Joint Enforcement Strike Force Brochure* ([DE 665](#))
 - *Information Sheet: Employment Enforcement Task Force* ([DE 631](#))

- *Information Sheet: Employment Development Department Underground Economy Operations ([DE 631UEO](#))*

The JESF member agency staff conducts outreach presentations to business and labor organizations throughout the state and to representatives of local government agencies.

Blatant Violations and Non-compliance

The EDD works with the JESF partner agencies to conduct joint on-site business inspections to identify employers who operate in the underground economy. The EDD also conducts desk investigations using various databases and income tax return analysis to detect non-compliance and fraud. When these inspections and investigations reveal non-compliance, the case is referred as an audit lead to the EDD's Tax Audit Program. In addition, the EDD receives audit leads from the IRS through the Questionable Employment Tax Practices (QETP) Program. On QETP audit leads that the IRS provides, the employers concurred with the IRS' findings regarding unreported wages and/or misclassified workers.

Employment Development Department Cumulative JESF Results

Following are the EDD's cumulative results from JESF inspections, investigations, and QETP leads, as well as the audit and collection actions stemming from JESF activities:

Calendar Year*	2013**	2014	2015	2016
Joint Inspections	807	614	583	600
EDD Audit Referrals	1,028	958	1,145	658
EDD Payroll Tax Audits Completed	491	686	664	512
EDD Payroll Tax Assessments on Above Audits	\$17,031,352	\$25,015,050	\$27,596,182	\$21,185,695
Previously Unreported Employees on Above Audits	6,912	11,354	9,981	6,329
Payroll Tax Assessments Collected	\$5,063,677	\$5,597,028	\$6,038,304	\$5,437,986

*Results fluctuate year-to-year based on the complexity of cases, staffing, and external lead referrals.

**Data is included for comparison purposes only. This data does not appear elsewhere in the report.

The following is additional information on the cumulative results from JESF activities:

Calendar Year*	2013**	2014	2015	2016
EDD Payroll Tax Audits with Fraud Penalty Assessed (included in figures above)	25	22	26	12
EDD Payroll Tax Assessments on Fraud Audits (included in figures above)	\$2,627,394	\$5,160,767	\$5,245,162	\$2,148,204
Previously Unreported Employees on Fraud Audits (included in figures above)	541	391	429	278

*Results fluctuate year-to-year based on the complexity of cases, staffing, and external lead referrals.

**Data is included for comparison purposes only. This data does not appear elsewhere in the report.

Criminal Tax Enforcement Program Results

For cases warranting criminal investigation, the EDD ID's Criminal Tax Enforcement Program works with law enforcement agencies and the JESF partner agencies throughout California to identify and prosecute those responsible for the criminal activities. Following are the EDD Criminal Tax Enforcement Program results for the calendar years 2014, 2015, and 2016:

Calendar Year*	2014		2015		2016	
Type of Action	# of Cases	Amount of Tax Liability	# of Cases	Amount of Tax Liability	# of Cases	Amount of Tax Liability
Payroll Tax Evasion Cases in Progress	182	\$90,716,914	187	\$99,915,619	139	\$93,844,110
EDD Criminal Complaints Filed	15	\$2,318,149	10	\$2,617,289	25	\$11,499,801
EDD Criminal Prosecutions Completed	35	\$9,318,288	51	\$56,650,246	7	\$1,667,143

*Results fluctuate year-to-year based on the complexity of cases, staffing, and external lead referrals.

Criminal Restitution Cases Monitored and Payments Received

When the court orders restitution to the EDD as part of the sentencing during criminal prosecutions, the EDD monitors these cases to ensure that the restitution is made.

Following are the results of restitution monitored for the calendar years 2014, 2015, and 2016:

Calendar Year	2014	2015	2016
Criminal Restitution Cases Monitored	37	79	84
Payments Received on Restitution Cases	\$773,621	\$1,022,994	\$329,584

Contractors' State License Board Legal Actions

Each month, the CSLB conducts stings and sweeps, which resulted in 1,647 legal actions for the calendar year 2016. As a result of the 756 licensee and non-licensee citations, the CSLB assessed \$607,930 in civil penalties.

Calendar Year	2014	2015	2016
Accusations	8	3	10
Administrative Licensee Citations	221	350	409
Criminal Referrals – Licensee	20	33	90
Criminal Referrals – Non-Licensee	463	743	791
Administrative Non-Licensee Citations	205	426	347
Total Legal Actions	917	1,555	1,647

Contractors' State License Board Stop Orders

In calendar year 2016, there were 436 stop orders served on construction employers, which prohibits the use of employee labor until workers' compensation insurance is obtained.

Calendar Year	2014	2015	2016
Licensee Stop Orders Issued	154	259	258
Unlicensed Operator Stop Orders Issued	169	231	178
Total Stop Orders Issued	323	490	436
Policies Obtained	93	200	165
Licenses Suspended	38	31	49

Contractors' State License Board Stings and Sweeps

The CSLB performed 84 stings and 243 sweeps during the calendar year 2016. The sting operations targeted unlicensed repeat offenders and wanted criminals who work in the construction industry. The stings involved the CSLB's Statewide Investigative Fraud Team inviting the suspected unlicensed contractors and wanted criminals to homes to place bids on home improvement projects. The suspects were found by searching advertisements on Craigslist and local Yellow Pages and leads from the CSLB's Intake Mediation Center. Construction site inspections or sweeps are also an effective way that the CSLB ensures contractor compliance with California's licensing and workers'

compensation insurance requirements. Investigators with CSLB's Statewide Investigative Fraud Teams fan out throughout the year with investigators from partner agencies, showing up unannounced at active construction sites to check for appropriate licenses, permits, workers' compensation insurance for employees, and adherence to safety rules.

Calendar Year	2014	2015	2016
Stings	72	91	84
Sweeps	82	148	243

United States Department of Labor Garment Industry Investigations

Following are results of the USDOL garment industry investigations in California for the last three calendar years.

Calendar Year	2014	2015	2016
Completed Investigations	219	182	265
Back Wages	\$2,117,134	\$1,763,682	\$3,604,675 (+ \$116,290 liquidated damages)
Civil Money Penalties	\$53,936	\$275,687	\$292,077
Number of Employees Affected	2,450	1,492	2,306

United States Department of Labor Recycling Center Investigations

Following are results of the USDOL recycling center investigations in California for the last three calendar years.

Calendar Year	2014	2015	2016
Completed Investigations	3	39	101
Back Wages	\$38,000 (+\$38,000 liquidated damages)	\$404,861 (+\$313,088 liquidated damages)	\$597,668 (+ \$509,121 liquidated damages)
Civil Money Penalties	\$3,003	\$0	\$0
Number of Employees Affected	13	288	288

Division of Labor Standards Enforcement Results

Following are results by industry of the Division of Labor Standards Enforcement JESF inspections for the last three calendar years.

	Number of Inspections			Number of Citations		
	2014	2015	2016	2014	2015	2016
Automotive	26	19	6	34	19	6
Car Wash	2	2	16	1	5	24
Construction	134	79	22	72	35	23
Garment	1	1	1	0	2	1
Other	161	101	74	137	87	101
Restaurant	73	78	58	80	87	56
Retail	34	24	16	50	27	12
Total	431	304	193	374	262	223

Total Dollar Amount of Penalties Assessed			
	2014	2015	2016
Automotive	\$264,645	\$205,807	\$33,331
Car Wash	\$1,500	\$27,300	\$161,520
Construction	\$512,623	\$178,080	\$77,300
Garment	0	\$6,050	\$1,900
Other	\$3,599,053	\$860,695	\$814,328
Restaurant	\$873,803	\$1,085,354	\$803,421
Retail	\$214,128	\$340,825	\$202,796
Total	\$5,465,752	\$2,704,111	\$2,094,595

License Suspensions/Holds Requested

The ability of state agencies to suspend/hold a license needed to legally operate certain types of businesses in this state is a valuable collection tool for resolving delinquent tax liabilities and for compelling corrective action. There are three types of licenses that the EDD can request other state agencies to suspend/hold if the licensee is delinquent in paying amounts due to the EDD:

- Contractor's License (CSLB Hold): The Business and Professions Code Section 7145.5 authorizes the CSLB to take disciplinary action against a license holder. Once the CSLB receives the request from the EDD to place a hold, the CSLB will suspend the license. In addition, the CSLB will search their database for all licenses with the same personnel of record and suspend those licenses as well. The licenses remain suspended until the delinquency that led to the suspension has been resolved or arrangements have been made to pay it.
- Liquor License (ABC Hold): The Business and Professions Code Section 24049 authorizes the EDD to request from the ABC a hold to be placed on certain types of liquor licenses. A hold establishes a priority for the EDD to any monies received from

the sale of the liquor license and prevents the transfer of a liquor license from the seller to a buyer until the conditions of the hold have been met.

- Farm Labor Contractor's License (FLC Hold): The EDD is authorized by Section 1141 of the CUIIC to notify the Labor Commissioner (of the DLSE) in writing that an FLC is delinquent in payment of worker contributions either by self-assessment or by a final EDD assessment. California Labor Code (LC) Section 1690.1 authorizes the Labor Commissioner to refuse to issue or renew any license until the licensee has fully paid the amount of the delinquency.

License Suspensions/Holds by Category Requested by the Employment Development Department for the Last Three Calendar Years

Type of Hold	2014	2015	2016
CSLB	365	631	557
ABC	63	111	88
FLC	11	8	15

Contractors' State License Board License Suspensions

A license can be suspended by the CSLB if the licensee is delinquent in paying amounts due to the CSLB or other state agencies. The table below summarizes amounts due to state agencies that were collected or resolved in calendar years 2014, 2015, and 2016 to avoid a license suspension or to have a suspended license unsuspended.

Calendar Year	Amounts Collected or Resolved		
	2014	2015	2016
CSLB	\$149,613	\$130,980	\$132,782
EDD	\$23,943,050	\$22,730,753	\$13,707,896
DIR-Cal/OSHA	\$265,788	\$815,684	\$784,421
DIR-DLSE	\$1,567,303	\$937,674	\$661,066
FTB	\$3,901,471	\$2,926,488	\$5,985,942
Totals	\$29,827,225	\$27,541,579	\$21,272,107

Information Sharing

Businesses that operate in the underground economy constantly develop new schemes to avoid detection of their illegal activities. As these new schemes are identified by the JESF members, information regarding the schemes is shared with member agencies, business associations, and labor organizations. There is an ongoing need for the JESF staff to be aware of the various types of schemes used in industries prone to underground economy activity. This knowledge transfer facilitates the development of detection and enforcement techniques necessary to stop the illegal activities. Information is shared as follows:

- On-the-job.
- Informal ad-hoc joint management meetings.

- Semi-annual meetings with member agencies.

During federal fiscal year 2016, the IRS completed audits of 18 *Employer's Quarterly Federal Tax Returns* (Forms 941) based on QETP leads the EDD provided to the IRS, resulting in assessments totaling \$29,275 in previously unreported federal taxes. The amount assessed represents reclassified payments (from independent contractor to employee), under-reported wages, and/or fringe benefits identified during the audits.

During calendar year 2016, the JESF began conducting supplemental meetings to share “best practices” of methods used to successfully collect amounts due from underground employers caught through enforcement efforts.

The enactment of Senate Bill 560 (Chapter 389, Statutes of 2015) further reinforced data sharing efforts between the DCA-CSLB and EDD by codifying a longstanding data sharing practice whereby the DCA provides the EDD with licensing and other information.

Collaboration

As the lead agency, the EDD participates in all JESF inspections. The other JESF partners participate in inspections when there is a potential violation of the laws they enforce. The table below highlights JESF collaboration efforts. It shows the number of business inspections that partner agencies participated in during calendar years 2014, 2015, and 2016.

Agency	Calendar Year		
	2014	2015	2016
EDD	614	583	600
DLSE	431	304	193
CSLB	161	183	303
Local Police	88	95	79
District Attorney	71	80	74
ABC	13	23	25
BOE	8	1	1
BAR	7	0	9
BSIS	3	8	13
CDI	*	*	49
FTB	*	*	25
Cal/OSHA	*	*	19
DMV	*	*	6
Other	159	96	64

* Participation by these entities was included in the “Other” category in calendar years 2014 and 2015.

The Interagency Tax Collection Committee is an alliance with the EDD, FTB, BOE, IRS, Attorney General, State Controller, and various county recorders. It provides a forum to

share common collection practices in order to increase compliance and resolve collection issues. It also allows the agencies to meet and share information about their collection programs, focusing on common, competing, and overlapping functions including bankruptcy, lien, and levy issues. It is intended to foster communications and allow collection staff to meet their counterparts, establish working relationships, and encourage cooperation on common tax collection issues.

The Interagency Tax Collection Committee formed the Liquor License Task Force consisting of representatives from the EDD, BOE, and FTB. The task force received and compiled recommendations from each agency on how to collaboratively handle the seizure and sale of liquor licenses. An interagency agreement was finalized in the fall of 2014. It establishes the procedures for the disbursement of funds and the release of transfer holds when liquor licenses issued by the ABC are seized and sold by one of the state tax agencies.

On May 18, 2016, the CDI led a statewide enforcement outreach focused on providing information to businesses that may operate in California's multi-billion dollar underground economy. The multi-agency team, which included the CSLB, EDD, FTB, DIR, and local district attorneys visited dozens of locations across the state to educate business owners of their obligations to comply with insurance, licensing, workplace safety, labor laws, and tax codes. Safety, licensing, and insurance violations were found at approximately 20 of the businesses visited. Some were found to not have required licenses or workers' compensation insurance and were issued immediate stop work orders. Others received administrative citations and penalties for workplace safety violations and some received audit referrals.

During the past several years, Memoranda of Understanding have been developed to facilitate the sharing of information and data between enforcement partner agencies and to enhance collaboration and joint enforcement of labor, tax, and licensing laws.

The Joint Enforcement Strike Force/Labor Enforcement Task Force Collaborative Enforcement Partnership

To help combat California's underground economy and protect workers' rights, the DIR and EDD have joined efforts through their respective enforcement programs, namely, the JESF and Labor Enforcement Task Force (LETF), to coordinate activity and share effective strategies.

The JESF/LETF Collaborative Enforcement Partnership merges best practices based on a wide range of experiences and innovation. The joint effort draws upon both programs' respective strengths through training, refinement of targeting methods, and strategic planning. While the JESF and LETF remain under the guidance of their respective agencies, enforcement coordination has allowed a streamlining of administration to leverage resources and mitigate overlap. The results include broader statewide operations, stronger communications, and knowledgeable, cross-trained staff.

The DIR hosted the third annual JESF/LETF joint training session in 2016; investigators and supervisors from around the state came together to share best practices on joint

enforcement operations. Additionally, the DIR hosted a series of webinar training sessions for JESF/LETF staff in 2016. The LETF produces its own annual report to the Legislature regarding its activities. The report can be found at www.dir.ca.gov.

BLATANT VIOLATOR CASES

The following examples of blatant violation cases detected by the JESF include the most flagrant cases where schemes were used by businesses to avoid payroll tax, labor, insurance, and licensing laws, and where the EDD found fraud or intent to evade payment of payroll taxes.

Blatant Violator Investigation Cases

- The EDD and USDOL conducted an inspection of a business that manufactures women's apparel. During the inspection, 45 workers were observed performing services. The company was registered with the EDD, but since its inception in 2013, only two employees were reported to the EDD. Interviews with workers revealed they were providing services six days a week and were paid cash at the end of each week. The cash wages were not reported to the EDD. A subsequent EDD audit revealed that the company did not keep proper accounting records. Further evidence was found indicating the company made deliberate acts and omissions to evade the payroll tax reporting requirements. The employer was aware of the reporting requirements since some of the employees were reported. The audit covered the period of 2012 to 2016. A fraud penalty was charged under Section 1128 of the CUIIC for intent to evade and failure to report all payments made to workers on Form W-2 or 1099. The company was assessed \$745,401 for unpaid payroll taxes, penalties, and interest.
- The EDD, DLSE, CDI, and Anaheim Police Department conducted an inspection of a massage parlor business. The owner has been in operation since 2011 and for a period of time operated in three locations. During the inspection it was found that the employer was not properly licensed to provide massage services. Interviews with workers indicated they received cash pay. The employer was cited by the DLSE for failure to maintain workers' compensation insurance and failure to provide itemized wage statements to the employees. A subsequent EDD audit revealed that the company had been operating and utilizing the services of massage therapists since 2011 but failed to register with the EDD until 2013. Once registered, the company filed state payroll tax returns, erroneously reporting zero wages for each quarter. However, the audit showed that the company made cash payments to its workers. The company also failed to maintain a record of the cash payments. The audit covered the period of 2011 to 2015. A fraud penalty was charged under Section 1128 of the CUIIC for intent to evade and failure to issue W-2's or 1099's to its workers. The company was assessed \$443,227 for unpaid payroll taxes, penalties, and interest.
- The EDD and DLSE conducted an inspection of a restaurant in response to an allegation of unreported cash pay and labor law violations from an employee of the restaurant. The business opened in 2011. It is a full service restaurant with 25 tables that seat two to eight customers per table. The restaurant also has a take-out menu and offers full service catering. The business was registered with the EDD and had workers' compensation insurance at the time of the inspection. A subsequent EDD

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audit revealed that although the business was registered and reporting wages to the EDD, not all of the wages paid to its employees were reported. The company did not maintain proper accounting records. During interviews with the owner, he admitted paying workers half of their pay by check and half in cash. He did not keep records of the cash payments and did not report the cash wages to the EDD. The wages paid by check were reported to the EDD and included on the employees' W-2's. The audit covered the period of 2011 to 2016. A fraud penalty was charged under Section 1128 of the CUIA for intent to evade and failure to report all payments made to all workers on Form W-2 or 1099. The company was assessed \$193,648 for unpaid payroll taxes, penalties, and interest.

- The EDD and CSLB's Statewide Investigative Fraud Team conducted an inspection of a construction business operating as a sole proprietorship. The inspection team observed six workers performing work in the backyard of a residential home. The workers were interviewed in Spanish but were hesitant to talk. The owner was also interviewed. He indicated that the workers were employees and were paid by check. The company was not registered with the EDD at the time of the inspection. A subsequent EDD audit revealed that the company had been operating since 2013 and had a valid license as a general contractor. Although the owner had stated during the inspection that workers were being paid by check, when the auditor reviewed the bank statements and cancelled checks, no records of payments to the workers were found. However, the business's income tax returns indicated the company claimed large labor expenses. It was determined the workers had been paid in cash and the wages had not been reported to the EDD. A fraud penalty was charged under Section 1128 of the CUIA for intent to evade and failure to report all payments made to workers on Form W-2 or 1099. The company was assessed \$110,368 for unpaid payroll taxes, penalties, and interest.

Joint Criminal Prosecution Cases

The JESF member agencies refer cases to their respective criminal investigation organizations. The following are cases that the JESF member agencies worked together to prosecute in 2016.

- The ID participated in a joint investigation with the Los Angeles County District Attorney's Office and the CDI against a clothing manufacturer. The employer and their Certified Public Accountant had misclassified employees and not reported the true payroll to the EDD and a workers' compensation insurance carrier. The employment tax liability owed to the EDD was \$2,869,176. The first defendant and the Certified Public Accountant each pleaded no contest to two counts of workers' compensation insurance fraud. A third defendant was convicted of two counts of failure to pay state payroll taxes. Sentencing was scheduled for a future date.
- The ID conducted a joint criminal investigation with the CDI of a nail salon employer who failed to report and underreported employee wages to the EDD and to workers' compensation insurance carriers. The employer intentionally misclassified employees as independent contractors. The employment tax liability owed to the

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EDD was \$149,708. The first of two defendants pleaded guilty to misdemeanor violations involving the CUIC and California Insurance Code (CIC). The second defendant was convicted of one misdemeanor count involving violation of the CIC. Both defendants were placed on three years of formal probation and sentenced to 40 days in jail. The employer was ordered to pay restitution to the EDD and the workers' compensation insurance carriers.

- The ID conducted a joint criminal investigation with the Santa Clara District Attorney's Office of a roofing contractor who was committing workers' compensation insurance premium fraud by reporting employees only after they were injured on the job. The investigation revealed the employer failed to report all employees and their wages to the EDD. An audit identified \$575,440 in wages that were not reported to the EDD between January 1, 2009 and December 31, 2012. The employment tax liability owed to the EDD was \$146,879. The first of two defendants pleaded no contest to 13 felony counts including violations of the CUIC. The first defendant was sentenced to three years of formal probation. The second defendant pleaded no contest to three felony counts involving violation of the CUIC. The second defendant was sentenced to seven years and four months of probation. The charges were later reduced to misdemeanors and both defendants were ordered to pay restitution jointly and severally to the FTB and State Compensation Insurance Fund (SCIF). The defendants were also ordered to pay investigation costs to the EDD.
- The ID conducted a joint criminal investigation with the CDI of a paving contractor in Sacramento County. An EDD audit uncovered \$1,092,842 in wages that were not reported to the EDD from the fourth quarter of 2012 through the second quarter of 2015. The employment tax liability owed to the EDD was \$115,922. The employer also failed to accurately report employees to workers' compensation insurance carriers.
The defendant pleaded guilty to felony counts involving the CIC and CUIC and was sentenced to serve one year in county jail, five years of formal probation, and to make restitution payments to two insurance carriers and the EDD.
- The ID conducted a joint investigation with the CDI of a construction company in Los Angeles that was making cash payments to unreported workers to evade employment tax and workers' compensation insurance payments. The employment tax liability owed to the EDD was \$109,168. The employer pleaded guilty to felony charges involving violation of the CIC and CUIC. The court ordered the defendant to pay the EDD full restitution including the cost of the investigation.
- The ID conducted a joint investigation with the Santa Clara County District Attorney's Office of a building contractor who underreported wages paid to employees. The employment tax liability owed to the EDD was \$96,326. The employer pleaded no contest to one misdemeanor charge involving violation of the CIC and one felony charge involving violation of the CUIC. The employer paid full restitution during the proceedings and sentencing was scheduled for a future date.

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- The ID conducted a joint investigation with the Tehama County District Attorney's Office, SCIF, and CDI of a reforestation contractor who failed to report employee wages to the SCIF during 2012. The employer withheld payroll taxes from the wages of employees but did not report the wages or pay the taxes to the EDD and did not pay the required workers compensation insurance premiums. The tax liability owed to the EDD was \$81,378. The defendant pleaded no contest to two felony counts involving violations of the CIC and CUIC. A restitution hearing has been scheduled regarding the amount due to the EDD.
- The ID conducted a joint investigation with the Santa Barbara County District Attorney's Office of a slurry seal coating contractor. The employer failed to report all of his employees and their wages to the EDD. An audit identified \$2,029,758 in unreported wages paid to employees between April 1, 2013 and December 31, 2014. The employment tax liability owed to the EDD was \$65,164. The employer pleaded guilty to charges involving violation of the California LC, CUIC, CIC, and California R&TC. Sentencing was scheduled for a future date.
- The ID conducted a joint investigation with the Orange County District Attorney's Office of a heating and air conditioning contractor who failed to pay taxes to the EDD and prevailing wages for work performed on two public works contracts. The employment tax liability owed to the EDD was \$31,161. The employer was previously convicted of nine counts of violating the CUIC. The remaining counts, out of a total of 37, included violations of taking and receiving a portion of workers' wages on public works, forgery, recording false and forged instruments, and willful failure to pay tax. During October of 2016, the employer was sentenced to 365 days in county jail and was ordered to serve five years of formal probation.

ATTACHMENT B

ACRONYMS

ABC	California Department of Alcoholic Beverage Control
BAR	Bureau of Automotive Repair
BOE	Board of Equalization
BSIS	Bureau of Security and Investigative Services
Cal/OSHA	Division of Occupational Safety and Health
CDI	California Department of Insurance
CIB	Criminal Investigation Bureau
CIC	California Insurance Code
CSLB	Contractors' State License Board
CUIC	California Unemployment Insurance Code
DCA	Department of Consumer Affairs
DIR	Department of Industrial Relations
DI	Disability Insurance
DLSE	Division of Labor Standards Enforcement
DMV	Department of Motor Vehicles
DOSH	Division of Occupational Safety and Health
EDD	Employment Development Department
FLC	Farm Labor Contractor
FTB	Franchise Tax Board
ID	Employment Development Department, Investigation Division
IRS	Internal Revenue Service
JESF	Joint Enforcement Strike Force
LC	California Labor Code
LETF	Labor Enforcement Task Force
PC	California Penal Code
QETP	Questionable Employment Tax Practices
R&TC	Revenue and Taxation Code
SCIF	State Compensation Insurance Fund
UI	Unemployment Insurance
USDOL	United States Department of Labor



**Edmund G. Brown Jr.
Governor
STATE OF CALIFORNIA**

**David M. Lanier
Secretary
LABOR AND WORKFORCE DEVELOPMENT AGENCY**

**Patrick W. Henning
Director
EMPLOYMENT DEVELOPMENT DEPARTMENT**